

Message Text

CONFIDENTIAL

PAGE 01 LONDON 11618 01 OF 03 141744Z
ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 AID-05 CIAE-00 COME-00
EB-07 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00
XMB-02 OPIC-03 SP-02 LAB-04 EPG-02 SIL-01 OMB-01
CEA-01 STR-04 DODE-00 PM-04 H-01 L-03 NSC-05
PA-01 PRS-01 SS-15 /091 W
-----054735 141835Z /42

P 141725Z JUL 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 6127

INFO AMEMBASSY BONN PRIORITY

AMEMBASSY BRUSSELS PRIORITY

AMEMBASSY COPENHAGEN PRIORITY

AMEMBASSY DUBLIN PRIORITY

AMEMBASSY THE HAGUE PRIORITY

AMEMBASSY LUXEMBOURG PRIORITY

AMEMBASSY ROME PRIORITY

AMEMBASSY PARIS PRIORITY

USMISSION NATO PRIORITY

AMCONSUL BELFAST

AMCONSUL EDINBURGH

C O N F I D E N T I A L SECTION 01 OF 03 LONDON 11618

USEEC ALSO FOR EMBASSY

USOECD ALSO FOR EMBASSY

PASS LABOR, TREASURY, FRB

E.O. 11652: GDS

TAGS: PGOV, PINT, ELAB, UK

SUBJECT: THE END OF INCOMES POLICY AND THE CALLAGHAN
GOVERNMENT

REF: A) LONDON 11117; B) LONDON 11237; C) LONDON 11591

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 LONDON 11618 01 OF 03 141744Z

SUMMARY - RETURNING TO THE ANALYTICAL FRAMEWORK DESCRIBED
IN REF A, IT IS EVIDENT THAT THE ABSENCE OF A THIRD YEAR
OF VOLUNTARY PAY RESTRAINT (REF B) WILL HAVE A DESTABIL-
IZING EFFECT ON THE CALLAGHAN GOVERNMENT. WHILE THE
TERMS OF THE TRANSITION FROM THE PHASE II VOLUNTARY PAY
RESTRAINT TO A LESS CONSTRAINED COLLECTIVE BARGAINING
SITUATION HAVE YET TO BE DETERMINED -- AND THEY WILL BE

OF PIVOTAL IMPORTANCE -- IT IS ALREADY POSSIBLE TO IDENTIFY THE VARIABLES UPON WHICH THE TRANSITION WILL IMPACT MOST HEAVILY AND TO DISCERN POTENTIAL PROBLEM AREAS. EVEN THOUGH THE ECONOMIC MODEL (REF C) INDICATES THAT A MASSIVE "WAGES EXPLOSION" IS UNLIKELY, RECENT DEVELOPMENTS SEEM TO THREATEN THE LIBERAL PACT AND LABOR PARTY COHESION. THE CHANCES THAT RELATIONS BETWEEN THE GOVERNMENT AND THE TUC WILL DETERIORATE ARE ALSO INCREASED. THE EXTENT TO WHICH THESE TENDENCIES WILL AFFECT THE PROGRESS OF "POLITICAL ROT" AND THE GOVERNMENT'S PROPENSITY FOR POLITICAL MISCALCULATION, AS YET, IS PROBLEMATICAL. THE GOVERNMENT'S POLITICAL VULNERABILITY, HOWEVER, MUST BE JUDGED TO HAVE INCREASED, ALTHOUGH AN EARLY ELECTION IS NOT YET A PROBABILITY. END SUMMARY.

1. RECENT EVENTS HAVE ENDED HOPES FOR A THIRD YEAR OF VOLUNTARY PAY RESTRAINT ON THE PART OF THE UNIONS (REF B). THE NATURE OF THE TRANSITION FROM THE SECOND YEAR OF PAY RESTRAINT TO A LESS CONSTRAINED COLLECTIVE BARGAINING SITUATION WILL BE OF CENTRAL IMPORTANCE TO THE CALLAGHAN GOVERNMENT, AS WELL AS TO THE BRITISH ECONOMY. THE GOVERNMENT HAS NOT YET DETERMINED ITS POLICIES IN THE ABSENCE OF A PHASE III ACCORD; INDEED THERE IS CURRENTLY NO CONSENSUS IN THE CABINET AS TO HOW IT SHOULD PROCEED (SEPTTEL). THE VARIOUS POLITICAL

CONFIDENTIAL

PAGE 03 LONDON 11618 01 OF 03 141744Z

REACTIONS TO AN AS YET UNDEFINED GOVERNMENT POLICY, OF COURSE, CANNOT BE PREDICTED. EVEN THOUGH THE SHAPE OF THE TRANSITION PHASE IS NOT YET DISCERNABLE, THERE IS LITTLE DOUBT THAT RECENT DEVELOPMENTS AND THEIR CONSEQUENCES WILL IMPACT ADVERSELY ON THE CALLAGHAN GOVERNMENT, INCREASING INTERNAL AND EXTERNAL PRESSURES ON IT.

2. REF A DESCRIBED AN ANALYTICAL FRAMEWORK FOR ASSESSING THE CALLAGHAN GOVERNMENT'S POLITICAL PROSPECTS. IDENTIFYING SIX CRITICAL AND INTERRELATED VARIABLES -- COHESION OF THE LABOR PARTY; DURABILITY OF THE LIBERAL PACT; PROGRESS OF POLITICAL ROT WITHIN THE GOVERNMENT; THE POSSIBILITY OF POLITICAL MISCALCULATION; THE NATURE OF GOVERNMENT RELATIONS WITH THE TUC; AND THE STATE OF THE ECONOMY. THIS CABLE WILL EXAMINE THE WAYS IN WHICH THE FAILURE TO ACHIEVE A STAGE III PAY AGREEMENT MAY AFFECT THESE VARIABLES.

3. THE ECONOMIC MODEL DESCRIBED IN REF C SUGGESTS THAT A LARGE-SCALE "WAGES EXPLOSION" IS UNLIKELY TO RESULT FROM THE RETURN TO "FREE" COLLECTIVE BARGAINING. HOWEVER, AT LEAST SOME EXCESSIVE PAY

CLAIMS AND RELATED INDUSTRIAL ACTION CAN BE EXPECTED AND
THESE WOULD HAVE AN EFFECT ON THE RATE OF INFLATION.
UNEMPLOYMENT. INVESTMENT, AND PRODUCTION. UNDER THE BEST
OF CIRCUMSTANCES, SUCH DEVELOPMENTS COULD HARDLY HELP
CALLAGHAN ATTAIN THE LEVEL OF ECONOMIC RECOVERY HE WOULD

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 LONDON 11618 02 OF 03 141742Z
ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 AID-05 CIAE-00 COME-00
EB-07 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00
XMB-02 OPIC-03 SP-02 LAB-04 EPG-02 SIL-01 OMB-01
CEA-01 STR-04 DODE-00 PM-04 H-01 L-03 NSC-05
PA-01 PRS-01 SS-15 /091 W
-----054703 141836Z /42

P 141725Z JUL 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 6128

INFO AMEMBASSY BONN PRIORITY

AMEMBASSY BRUSSELS PRIORITY

AMEMBASSY COPENHAGEN PRIORITY

AMEMBASSY DUBLIN PRIORITY

AMEMBASSY THE HAGUE PRIORITY

AMEMBASSY LUXEMBOURG PRIORITY

AMEMBASSY ROME PRIORITY

AMEMBASSY PARIS PRIORITY

USMISSION NATO PRIORITY

AMCONSUL BELFAST

AMCONSUL EDINBURGH

C O N F I D E N T I A L SECTION 02 OF 03 LONDON 11618

SEEM TO NEED TO REALIZE HIS LONGER-TERM POLITICAL GOAL
-- THE REELECTION OF A LABOR GOVERNMENT. THESE FACTORS
WILL ALSO IMPINGE DIRECTLY ON THE OTHER KEY POLITICAL
VARIABLES. THUS THE FAILURE TO GAIN A THIRD YEAR OF
VOLUNTARY PAY RESTRAINT FROM THE UNIONS MUST BE CON-
SIDERED A SETBACK IN BOTH SHORT- AND LONG-RANGE TERMS,
EVEN THOUGH THE ECONOMIC LIMITS OF THE REVERSE REMAIN
UNDEFINED.

4. WE CANNOT YET PREDICT HOW THE ABSENCE OF A PHASE III

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 LONDON 11618 02 OF 03 141742Z

AGREEMENT WILL INFLUENCE THE GOVERNMENT/TUC RELATIONSHIP. IF THE TRANSITION SHOULD TURN OUT TO BE ORDERLY AND SERIOUS CONFRONTATION AVOIDED, THE SHORT-TERM RELATIONSHIP COULD BE STRENGTHENED. THE RETURN TO A LESS CONSTRAINED BARGAINING SITUATION COULD REVERSE CURRENT ATTITUDES AMONG UNION VOTERS WHICH ARE FAVORABLE TO THE CONSERVATIVES, AS NEW SETTLEMENTS CAN BE EXPECTED TO BEGIN TO RESTORE DIFFERENTIALS AND ELIMINATE OTHER ANOMOLIES WHICH OCCURRED UNDER PHASES I AND II. OTHER FACTORS, HOWEVER, ARE AT PLAY. IF THE GOVERNMENT TAKES A TOUGH LINE ON PAY INCREASES FOR PUBLIC EMPLOYEES (ABOUT 40 PERCENT OF THE WORK FORCE), TRYING TO HOLD THEM AT ABOUT 5 PERCENT, AND TRIES TO KEEP THE LID ON PRIVATE AND PUBLIC SECTOR WAGE SETTLEMENTS BY HOLDING MONETARY GROWTH IN LINE WITH ITS IMF COMMITMENTS. RELATIONS BETWEEN THE GOVERNMENT AND PUBLIC SECTOR UNIONS COULD DETERIORATE SHARPLY. THE TUC COULD WELL BE DRAWN INTO ANY SUCH CONFLICT. IF ACCOMPANIED BY WIDESPREAD STRIKES IN THE PRIVATE SECTOR. THE RELATIONSHIP COULD BREAK DOWN. CONFRONTATION COULD ALSO OCCUR IF THE GOVERNMENT SEEKS TO IMPOSE A RIGID WAGES POLICY BY STATUTE OR OTHER MEANS.

5. THE FAILURE OF THE GOVERNMENT AND THE TUC TO REACH A PHASE III ACCORD HAS ALREADY INCREASED THE STRESS BETWEEN THE LIBERALS AND THE GOVERNMENT. LIBERAL ECONOMIC SPOKESMAN JOHN PARDOE HAS PUBLICLY REAFFIRMED THE LIBERAL DEMAND FOR A STATUTORY PAY POLICY -- THE LIBERALS APPARENTLY FAVOR A FORM OF PRICE CONTROL WHICH WOULD PREVENT INDUSTRY FROM PASSING ON EXCESSIVE WAGE INCREASES IN THE FORM OF HIGHER PRICES, COUPLED WITH A TAX STRUCTURE THAT WOULD "CLAW BACK" EXCESSIVE WAGE GAINS FROM WORKERS. ALTHOUGH PARDOE'S STATEMENT MAY ACCU-
CONFIDENTIAL

CONFIDENTIAL

PAGE 03 LONDON 11618 02 OF 03 141742Z

RATELY REFLECT THE THEORETICAL LIBERAL POSITION, IT APPEARS UNLEAVENED BY HIS COLLEAGUES' INSTINCT FOR POLITICAL SURVIVAL AND WOULD PROBABLY BE POLITICALLY FATAL FOR THE GOVERNMENT. UNLESS WAGE CLAIMS WON BETWEEN AUGUST (WHEN SETTLEMENTS WILL NO LONGER BE MADE UNDER PHASE II) AND NOVEMBER (WHEN THE GOVERNMENT/LIBERAL PACT IS DUE FOR RENEWAL) ARE CLEARLY EXCESSIVE, WE ARE INCLINED TO BELIEVE THE LIBERAL INSTINCT FOR SURVIVAL WILL PREVAIL AND THE PACT RENEWED. THE ABSENCE OF A

PHASE III AGREEMENT, HOWEVER, MEANS THAT ANY NEW PACT
WILL BE FRAGILE.

6. THE ABSENCE OF PHASE III AGREEMENT, AT ONE LEVEL,
SHOULD DAMPEN INTERNAL STRESS WITHIN THE PLP. THE
DIMINUTION OF CURRENT PAY ANOMOLIES THROUGH NEWLY-
NEGOTIATED WAGE SETTLEMENTS WILL REMOVE AN IMPORTANT
SOURCE OF IRRITATION. BUT THIS BENEFICIAL POLITICAL
EFFECT MAY BE MORE THAN OFFSET BY TIGHT CONTROLS ON
PUBLIC SECTOR WAGES, WHILE HIGHER RATE OF INFLATION
AND GROWING UNEMPLOYMENT RESULTING FROM EXCESSIVE WAGE

CONFIDENTIAL

NNN

CONFIDENTIAL

PAGE 01 LONDON 11618 03 OF 03 141753Z
ACTION EUR-12

INFO OCT-01 ISO-00 EURE-00 AID-05 CIAE-00 COME-00
EB-07 FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00
XMB-02 OPIC-03 SP-02 LAB-04 EPG-02 SIL-01 OMB-01
CEA-01 STR-04 DODE-00 PM-04 H-01 L-03 NSC-05
PA-01 PRS-01 SS-15 /091 W
-----054824 141834Z /42

P 141725Z JUL 77

FM AMEMBASSY LONDON

TO SECSTATE WASHDC PRIORITY 6129

INFO AMEMBASSY BONN PRIORITY

AMEMBASSY BRUSSELS PRIORITY

AMEMBASSY COPENHAGEN PRIORITY

AMEMBASSY DUBLIN PRIORITY

AMEMBASSY THE HAGUE PRIORITY

AMEMBASSY LUXEMBOURG PRIORITY

AMEMBASSY ROME PRIORITY

AMEMBASSY PARIS PRIORITY

USMISSION NATO PRIORITY

AMCONSUL BELFAST

AMCONSUL EDINBURGH

C O N F I D E N T I A L SECTION 03 OF 03 LONDON 11618

SETTLEMENTS WOULD ALSO ACCENTUATE INTERNAL DIVISION
WITHIN THE PLP. THUS RELATIVELY LARGE PAY CLAIMS ARE

LIKELY TO REDUCE PLP COHESION, PARTICULARLY ON ECONOMIC ISSUES. ANY DETERIORATION IN THE GOVERNMENT'S RELATIONSHIP WITH THE TUC WOULD ALSO WEAKEN THIS COHESION. WHILE THE FINAL BALANCE WILL DEPEND ON THE WAY THE TRANSITION WORKS OUT IN PRACTICE, THERE IS NO DOUBT THAT THE ABSENCE OF A PHASE III AGREEMENT IS POTENTIALLY DAMAGING TO PLP COHESION.

CONFIDENTIAL

CONFIDENTIAL

PAGE 02 LONDON 11618 03 OF 03 141753Z

7. IT IS NOT YET CLEAR HOW THE TRANSITION WILL IMPINGE ON THE "POLITICAL ROT" AND POLITICAL MISJUDGMENT FACTORS. ARGUABLY, A SMOOTH TRANSITION TO UNRESTRAINED COLLECTIVE BARGAINING WOULD REDUCE THE DANGER FROM BOTH FACTORS, BUT IT WOULD BE OVERLY SANGUINE TO ASSUME REENTRY WILL BE EASY. IF THE OPPOSITE ASSUMPTION IS MADE, PRESSURES ON THE GOVERNMENT ARE LIKELY TO INCREASE, PROBABLY INTENSIFYING THE SPREAD OF POLITICAL ROT AND THE GOVERNMENT'S PROPENSITY FOR POLITICAL MISCALCULATION.

8. OUR TENTATIVE ANALYSIS CLEARLY INDICATES THAT THE TUC'S INABILITY TO DELIVER ON A PHASE III AGREEMENT WILL PROBABLY IMPACT ADVERSELY ON AT LEAST FOUR OF THE SIX KEY VARIABLES WHICH WILL DETERMINE THE CALLAGHAN GOVERNMENT'S CAPACITY TO REMAIN IN POWER. ALTHOUGH WE CAN DO LITTLE MORE AT THIS POINT THAN IDENTIFY THOSE VARIABLES WHICH WILL BE MOST DIRECTLY AFFECTED, INDICATIONS ARE THAT CALLAGHAN'S POSITION, DESPITE HIS APPARENT PARLIAMENTARY ADVANTAGE, WILL BECOME MORE VULNERABLE. IT IS STILL PREMATURE TO PREDICT AN EARLY GENERAL ELECTION, BUT THAT POSSIBILITY IS DEFINITELY GREATER THAN IT WAS A FEW WEEKS AGO.

BREWSTER

CONFIDENTIAL

NNN

Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: WAGES, POLICIES, ECONOMIC RECOVERY, CENTRAL GOVERNMENT
Control Number: n/a
Copy: SINGLE
Sent Date: 14-Jul-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977LONDON11618
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: GS
Errors: N/A
Expiration:
Film Number: D770251-0247
Format: TEL
From: LONDON USEEC
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770758/aaaabxzw.tel
Line Count: 316
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 6f21d76b-c288-dd11-92da-001cc4696bcc
Office: ACTION EUR
Original Classification: CONFIDENTIAL
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 6
Previous Channel Indicators: n/a
Previous Classification: CONFIDENTIAL
Previous Handling Restrictions: n/a
Reference: 77 LONDON 11117, 77 LONDON 11237, 77 LONDON 11591
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 03-Mar-2005 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 1863418
Secure: OPEN
Status: NATIVE
Subject: THE END OF INCOMES POLICY AND THE CALLAGHAN GOVERNMENT
TAGS: PGOV, PINT, ELAB, UK
To: STATE
Type: TE
vdkgvwkey: odhc://SAS/SAS.dbo.SAS_Docs/6f21d76b-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009